

Retiree News & NOTES



STATE RETIREMENT
and PENSION SYSTEM
of MARYLAND

JANUARY 2006

VOL. 24 NO. 1

A Newsletter for Retirees from the State Retirement & Pension System of Maryland

Changing tax withholdings? Follow these handy tips

RETIREES WHO WISH TO UPDATE their tax withholding elections must file a combined *Federal and Maryland State Tax Withholding Request* (Form 766) covering both federal and state taxes.

Form 766 revokes all prior federal and state tax withholding elections. For example, if you previously requested federal and state tax withholdings and now submit a new request indicating only state tax, your prior federal tax withholdings will be cancelled. You must fill out both sections of the form *even if you wish to update only one portion of your withholdings*.

Under current federal law, you cannot only designate a specific dollar amount to be withheld for federal tax. However, you can designate an additional amount to be withheld on Part I, line 3 of Form 766, provided you indicated your marital status and number of allowances on line 2 of the form.

Form 766 can be found on our Web site at www.sra.state.md.us or requested by calling a retirement benefits counselor at 410-625-5555 or toll free 1-800-492-5909.

State Retirement Pick-up and your taxes

FOR ELIGIBLE RETIREES, Block 15 of the 1099-R form contains the amount of your tax deferred contributions made under the State Retirement Pick-up Program. This figure is important for Maryland State income tax preparation.

The State Pick-up Program is concerned with the employee pension plan contributions made while working. It provides for the deferral of federal taxes when the contributions are made, but makes them taxable when received in the pension. Since this program only defers federal taxes at the time the contributions are made, state income taxes were deducted. The consequence in retirement is that the state income tax is deferred until the pick-up contributions are recovered.

While most members participated in the pick-up program, your participation was determined by whether your employer elected to participate and by whether your pension plan required you to make an employee contribution.

FEDERAL TAXES

Since eligible members did not pay any federal taxes on their pick-up contributions during employment, taxes must be paid during retirement. You do not need to make any special entries on your federal tax form — the Retirement Agency has included your pick-up contributions when computing the taxable amount of your pension for federal tax purposes.

MARYLAND STATE TAXES

You have already paid Maryland State taxes on the pick-up contributions listed on your 1099-R. To avoid paying taxes twice, you must subtract the pick-up amount from your federal adjusted gross income shown on page 1 of your Maryland tax return (Form 502) as follows:

Enter your pick-up amount on line 14, entering code letter "r." This serves as a subtraction from your income which will reduce your taxable net income on line 22 (Form 502).

The subtraction is limited to the amount of pick-up contribution stated on the 1099-R or the taxable pension, whichever is less. The remainder of the pick-up amount is carried over to next year's taxes. When the pick-up amount reaches zero, "EP used" will be printed in the pick-up block on your 1099-R. This usually occurs within a few years after the date of retirement.

ATTENTION 2005 RETIREES

For members who retired in 2005, the W-2 form you receive from your former employer will show 1) your annual wages earned prior to retirement and 2) any State pick-up contributions made in 2005. This amount serves as an addition to State income for 2005. Enter this figure on line 3 of your Maryland tax return (Form 502).

System continues strong investment

THE STATE RETIREMENT AND PENSION SYSTEM OF MARYLAND'S investment fund returned a notable gain of 9.5% during fiscal year 2005, the System's second straight year of strong returns.

This is a summary of the System's activities for the year ending June 30, 2005. For more detailed information, the System's comprehensive annual financial report is available online at www.sra.state.md.us.

SYSTEM FINANCES

The System is responsible for properly administering the retirement, disability and death benefits for its members and retirees. The System's overall funding objective is to accumulate sufficient assets over time to meet these long-term benefit obligations as they become due.

Revenues

During fiscal year 2005, investment earnings were \$2.8 billion, while revenues from employer and member contributions were \$670 million and \$209 million, respectively. For fiscal year 2005, member contribution rates remained unchanged, while employer rates varied depending on the System.

REVENUES

Employer Contributions	
2005	\$670 million
2004	\$632 million
Employee Contributions	
2005	\$209 million
2004	\$204 million
Net Investment Income	
2005	\$2.8 billion
2004	\$4.2 billion

Under the experienced direction of its Board of Trustees, the System plans to continue following its steady course toward maximizing investment returns while maintaining an acceptable level of risk.

Expenses

Retirement allowances paid to retirees and beneficiaries totaled \$1.7 billion in fiscal year 2005, which included \$19.2 million paid to members and withdrawing employers as a result of employment terminations, system transfers or withdrawal. Expenses for management of the investment portfolio and administration of the System were \$103 million and \$22 million, respectively.

EXPENSES

Benefit Payments	
2005	\$1.7 billion
2004	\$1.6 billion
Refunds	
2005	\$19 million
2004	\$12 million

Funded Status

As of June 30, 2005, the System's actuarial accrued liability was \$39.1 billion. With the actuarial value of assets accumulated to pay the liability at \$34.5 billion, the System now stands at 88.21% funded. The System remains financially strong and ahead of schedule with regard to its long-term funding goals.

Investments

The System continued to experience strong investment gains during the fiscal year with returns of 9.5%.

Annualized returns for the three, five, and 10-year periods ending June 30 were 9.5%, 1.9% and 7.6%, respectively. The market value of System assets increased from \$30.2 billion on June 30, 2004 to \$32.1 billion on June 30,

ent gains in fiscal '05

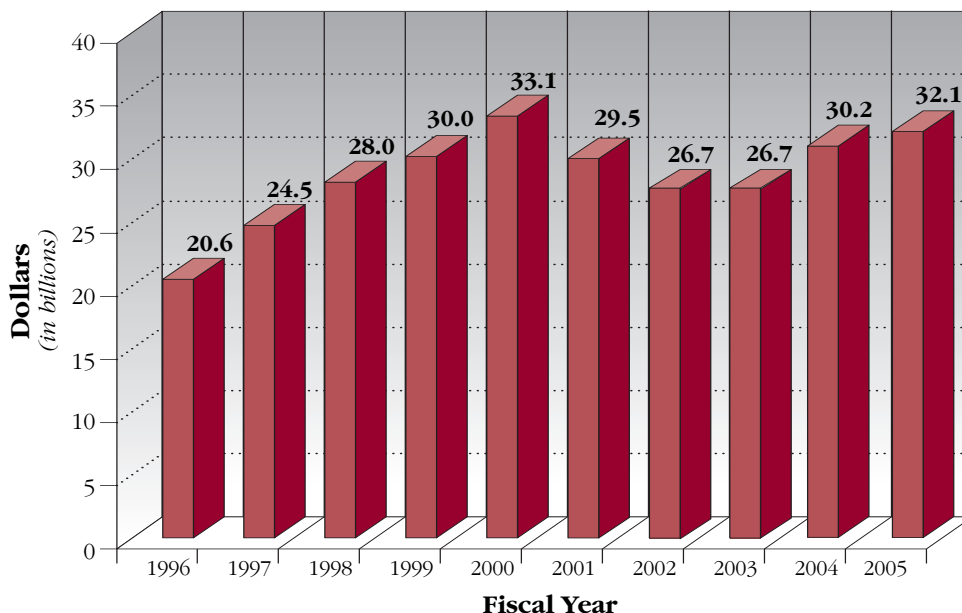
2005. The System's equity investments returned 8.8%, with U.S. equities returning 6.9% and international equities returning 14.0%. The System's fixed income investments returned 7.8%, and real estate returned 27.5%.

Under the experienced direction of its Board of Trustees, the System plans to continue following its steady course toward maximizing investment returns while maintaining an acceptable level of risk.

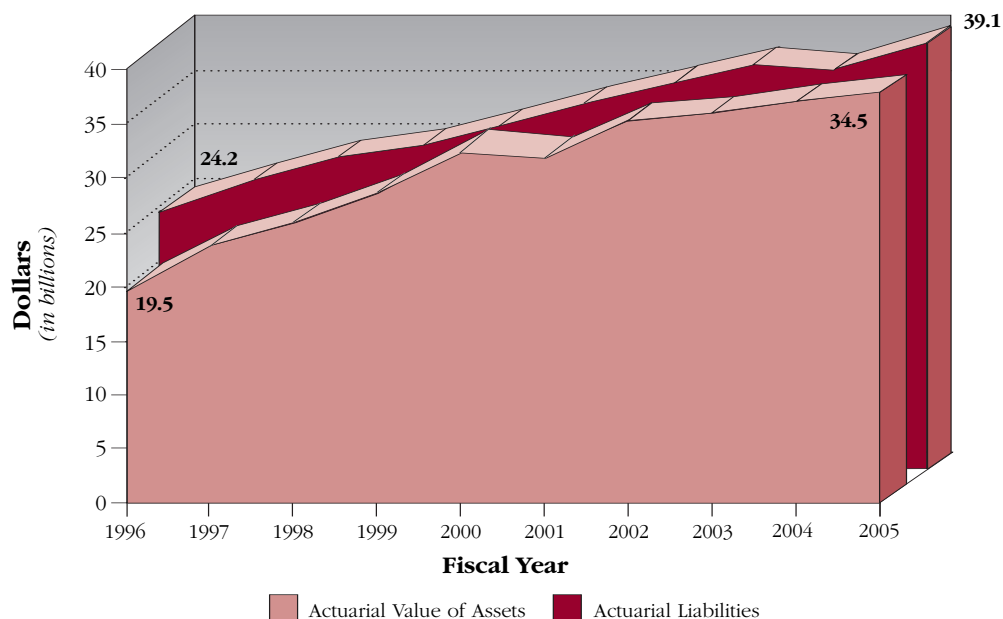
Membership

The System's rolls included 188,050 active members as of June 30, 2005, an increase of 2,189 members from the previous year. The System also served 100,196 retirees and beneficiaries at the end of fiscal year 2005, an increase of 5,316 over the previous year. From June 30, 2004 to June 30, 2005, the number of former members who are eligible for a future benefit (i.e., vested members) increased by 753 to a total of 47,664.

TEN-YEAR GROWTH OF INVESTMENT PORTFOLIO



TEN-YEAR HISTORY OF FUNDING PROGRESS



FOR MORE INFORMATION ...

The System's Comprehensive Annual Financial Report for fiscal year 2005 is available in its entirety online. Visit the State Retirement Agency Web site at www.sra.state.md.us to access a printable version of the report.

Understanding your 1099-R

PERSONALIZED COPIES of Internal Revenue Service Form 1099-R will be distributed to all State Retirement and Pension System retirees by the end of January, 2006. The forms provide each retiree with detailed information on his or her pension income for the previous year. Most retirees receive only one 1099-R each year. However, members who retired in 2005 will receive a separate form 1099-R for any additional refunds they received, such as a refund of State pick-up contributions or a refund of voluntary annuity contributions.

HOW TO READ YOUR 1099-R

BLOCK 1.

(GROSS DISTRIBUTION)

This is the total amount of pension benefits paid to you by the State Retirement Agency during the 2005 calendar year.

BLOCK 2A.

(TAXABLE AMOUNT)

This is the taxable amount of your pension. Depending on your retirement date and whether you contributed to your plan, you may not be taxed on the total amount of benefits paid to you. If this is the case, the amount shown in this block will differ from the amount in Block 1.

BLOCK 2B.

(TAXABLE AMOUNT NOT DETERMINED)

This block applies *only* to disability retirees who retired prior to January 1, 1995. These individuals should consult IRS Publication 575 before preparing their tax returns.

BLOCK 4.

(FEDERAL INCOME TAX WITHHELD)

This block shows any federal income tax deducted from your monthly retirement checks. To change the amount of federal income tax being withheld, complete a tax withholding request form (Form 766), available through the State Retirement Agency.

BLOCK 5.

(EMPLOYEE CONTRIBUTIONS)

This is the amount of your contributions that were recovered, tax free, during 2005. This figure is the difference between the amounts in Blocks 1 and 2a. The dollar figure in this box does NOT represent the amount of any health insurance premiums withheld from your benefit payment.

BLOCK 7.

(DISTRIBUTION CODE)

IRS codes are explained on the back of the 1099-R form.

BLOCK 9B.

(TOTAL EMPLOYEE CONTRIBUTIONS)

For retirees who received their first benefit payments in 2005, this block contains the value of any contributions made during employment that can be recovered tax-free. Only members who retired in 2005 and made pension contributions will see

a value in this block. For members who retired prior to 2005, a zero will be printed in the block.

BLOCK 10.

(STATE INCOME TAX WITHHELD)

Any Maryland State income tax deducted from your monthly checks is shown in this block. To change the amount being withheld, complete a tax withholding request form (Form 766).

BLOCK 15.

(PICK-UP CONTRIBUTIONS)

This figure applies to members whose employers participated in the State Pick-up Program. For an explanation of pick-up contributions, see "State Retirement Pick-up and your taxes" on page 1.

DUPLICATE 1099-R

To request a duplicate copy of your 1099-R form, please call the State Retirement Agency at 410-625-5555 or 1-800-492-5909.

Form 1099-R

2005

VOID **CORRECTED**

OMB No. 1545-0119

Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.

Copy C For Recipient's Records

This information is being furnished to the Internal Revenue Service.

Department of the Treasury - Internal Revenue Service

(Keep for your records.)

PAYER'S name, street address, city, state, and ZIP code
 MARYLAND STATE RETIREMENT AGENCY
 120 EAST BALTIMORE STREET
 BALTIMORE, MD 21202-6700

1 Gross distribution
 \$ 12,000.00

2a Taxable amount
 \$ 11,000.00

2b Taxable amount not determined ☐ **Total distribution** ☐

3 Capital gain (included in box 2a)
 \$.00

4 Federal income tax withheld
 \$ 500.00

5 Employee contributions or insurance premiums
 \$ 1,000.00

6 Net unrealized appreciation in employer's securities
 \$.00

7 Distribution code
 7

8 Other
 \$.00

9a Your percentage of total distribution
 %

9b Total employee contributions
 \$ 16,868.75

10 State tax withheld
 \$ 250.00

11 State/Payer's state no.
 MARYLAND
 52-6104406

12 State distribution
 \$.00

13 Local tax withheld
 \$.00

14 Name of locality
 \$ 3,000.00

15 Pick-Up Contrib's
 \$.00

PAYER'S Federal identification number
 52-6104406

RECIPIENT'S identification number
 123-45-6789

Account number (optional)

MARY SMITH
 123 MAIN STREET
 BALTIMORE, MD 21201

Form 1099-R

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